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Department of the Treasury
Washington, DC 20224

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Person To Contact:

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PLR-102825-21

Date:

August 09, 2021

Legend

Decedent
Spouse
Marital Share
Trust
Date 1
Date 2
Date 3
a
State
State Statute

Dear :

This letter responds to your authorized representative's letter dated January 26, 2021, and subsequent correspondence, requesting income, estate, and gift tax rulings with respect to the proposed division of Trust.

The facts and representations submitted are summarized as follows:

Decedent established Trust, a revocable trust, on Date 1. Trust was most recently restated on Date 2. Trust is governed under the law of State.

Article First of Trust provides, in relevant part, that Trust is to be irrevocable upon Decedent's death. Decedent is to be the initial trustee of Trust, and if Decedent is unable or unwilling to serve (or continue to serve) as trustee, Spouse, Decedent's spouse, is to serve as trustee.

Article Second provides, in relevant part, that so long as Decedent is living, the trustee has full and absolute discretion to distribute Trust income to Decedent.

Article Third provides, in relevant part, that at the death of Decedent, Trust is to continue but the trustee is to divide the Trust assets into two shares. One share, known as the By-Pass Share, is to be funded with assets equal in value to the applicable exclusion amount, less lifetime gifts and renunciations chargeable against the exclusion. The trustee of the By-Pass Share is to pay to or expend on behalf of Spouse, the net income derived from the By-Pass Share for Spouse's health, education, maintenance, and support, in accordance with his standard of living and financial resources. In the event the net income from the By-Pass Share is insufficient to meet that standard, the trustee is to have the power to encroach upon the corpus of the By-Pass Share to an extent necessary for Spouse's health, education, maintenance, and support. By-Pass Share is to terminate upon Spouse's death.

Article Fourth provides, in relevant part, that at the death of Decedent, after funding the By-Pass Share, the remainder of the assets constituting Trust property is to fund Marital Share. Marital Share is for the exclusive benefit of Spouse and is irrevocable. Spouse is to serve as initial trustee of Marital Share. The trustee of Marital Share is to pay or expend on behalf of Spouse, at least annually or at more frequent intervals, all of the income derived from Marital Share. Spouse is granted the right to demand that the trustee invest in income producing assets with respect to Marital Share. Marital Share is to terminate at the death of Spouse.

Article Fifth provides, in relevant part, that at the death of Decedent and Spouse, the trustee is to distribute the remaining assets of the By-Pass Share and Marital Share equally to the trusts created for the benefit of Decedent's children.

Decedent died on Date 3, survived by Spouse and two children. Decedent's executor elected to treat Marital Share as qualified terminable interest property (QTIP) under § 2056(b)(7) of the Internal Revenue Code.

Spouse, as trustee of Marital Share, seeks to divide Marital Share into two separate, but identical, trusts, Trust A and Trust B. Trust A would be funded from Marital Share with assets having a net fair market value on the date of division equal in value to \$a, the basic exclusion amount under § 2010(c)(3) for the current year, and Trust B would be funded with all remaining cash and property of Marital Share.

The trustee, Spouse, and the beneficiaries of the trusts created for the benefit of Decedent's children agree that such a division will not impair the rights of any beneficiary or adversely affect achievement of the purposes of Marital Share. The division of the assets of Marital Share will be made on a pro-rata, fractional basis, by identifying the assets and liabilities passing to each separate trust. Further, the interests will continue to be held under identical terms in the assets of Marital Share through Trust A and Trust B before and after the division.

Following the division of Marital Share into Trust A and Trust B, Spouse will disclaim his interest in Trust A. As a consequence of Spouse's disclaimer, the assets in Trust A will be distributed to the trusts created for the benefit of Decedent's children, pursuant to Article Fifth of Trust.

State Statute provides, in relevant part, that a trustee may, unless expressly prohibited by the terms of the instrument establishing the trust, divide a trust into two or more separate trusts without a judicial proceeding if the result does not impair the rights of any beneficiary or adversely affect achievement of the purposes of the original trust. The trustee may make a division under this subsection by giving written notice of the division to each beneficiary who might then be entitled to receive distributions from the trust and by executing a written instrument stating that the trust has been divided pursuant to this section and that the notice requirements of this subsection have been satisfied. A trustee, in the written instrument dividing a trust, is to allocate trust property among the separate trusts on a fractional basis, by identifying the assets and liabilities passing to each separate trust.

You have requested the following rulings:

1. The division of Marital Share into Trust A and Trust B on a fractional basis will not cause Marital Share, Trust A, Trust B or any beneficiary of these three trusts to recognize ordinary income or loss, or capital gain or loss, under § 61 or § 1001.
2. After the division of Marital Share into Trust A and Trust B, Trust A and Trust B will continue to be QTIP trusts under § 2056(b)(7).
3. Upon Spouse's disclaimer of his interest in Trust A, Spouse will be treated as having made a gift of his qualifying income interest in Trust A under § 2511, and as having made a gift of all of the interests in Trust A other than the qualifying income interest under § 2519.
4. Spouse's disclaimer of his interest in Trust A will not cause any property in Trust B to be treated as a gift by Spouse under § 2519.
5. The value of the property in Trust A treated as transferred under § 2519 will not be included in Spouse's gross estate under § 2044(a) because of the application of § 2044(b)(2).
6. Spouse's disclaimer of his interest in Trust A will not cause his interest in Trust B to be valued at zero under § 2702.

Ruling 1

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

Section 1001(a) provides that the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in § 1011 for determining loss over the amount realized.

Section 1001(b) states that the amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received. Under § 1001(c), except as otherwise provided in subtitle A, the entire amount of gain or loss, determined under § 1001, on the sale or exchange of property shall be recognized.

Section 1.1001-1(a) of the Income Tax Regulations provides that the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially either in kind or in extent, is treated as income or loss sustained.

Section 1.1001-1(h)(1) provides that the severance of a trust is not an exchange of property for other property differing materially either in kind or in extent if -- (i) an applicable state statute or the governing instrument authorizes or directs the trustee to sever the trust, and (ii) any non-pro rata funding of the separate trusts resulting from the severance whether mandatory or in the discretion of the trustee, is authorized by an applicable state statute or governing instrument.

An exchange of property results in the realization of gain only if the properties exchanged materially differ. Cottage Savings Association v. Commissioner, 499 U.S. 554 (1991). A material difference exists when the exchanged properties embody legal entitlements “different in kind or extent” or if they confer “different rights and powers.” Id. at 565.

Rev. Rul. 56-437, 1956-2 C.B. 507, provides that a partition of jointly owned property pursuant to state law is not a sale or other disposition of property where the co-owners of the joint property sever their joint interests, but do not acquire a new or additional interest as a result of the transaction. Thus, neither gain nor loss is realized on a partition.

Accordingly, based on the facts presented and the representations made, we conclude that the division of Marital Share into Trust A and Trust B on a fractional basis

will not cause Marital Share, Trust A, Trust B or any beneficiary of these three trusts to recognize ordinary income or loss, or capital gain or loss, under § 61 or § 1001.¹

Ruling 2

Section 2001(a) imposes a tax on the transfer of the taxable estate of every decedent who is a citizen or resident of the United States.

Section 2056(a) provides that, except as limited by § 2056(b), the value of the taxable estate is to be determined by deducting from the value of the gross estate an amount equal to the value of any interest in property that passes or has passed from the decedent to the surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

Under § 2056(b)(1), a marital deduction is not allowable for an interest in property passing to the surviving spouse that is a "terminable interest." An interest passing to the surviving spouse is a terminable interest if it will terminate or fail on the lapse of time or on the occurrence of an event or contingency, or on the failure of an event or contingency to occur and, on termination, an interest in the property passes to someone other than the surviving spouse.

Section 2056(b)(7) provides an exception to the terminable interest rule in the case of qualified terminable interest property (QTIP). Under § 2056(b)(7), qualified terminable interest property is treated as passing to the surviving spouse for purposes of § 2056(a), and no part of the property is treated as passing to any person other than the surviving spouse for purposes of § 2056(b)(1). Section 2056(b)(7)(B)(i) provides that the term "qualified terminable interest property" means property: (i) which passes from the decedent; (ii) in which the surviving spouse has a qualifying income interest for life; and (iii) to which an election under § 2056(b)(7)(B)(v) applies.

Section 2056(b)(7)(B)(ii) provides that the surviving spouse has a qualifying income interest for life if (I) the surviving spouse is entitled to all the income from the property, payable annually or at more frequent intervals and (II) no person has a power to appoint any part of the property to any person other than the surviving spouse.

In this case, after the division of Marital Share into Trust A and Trust B, Spouse will continue to be entitled to all the income from the property, payable annually or at more frequent intervals in the trusts. Further, no person, other than Spouse, will have a power to appoint any part of the property in the trusts to any person other than Spouse. Accordingly, Spouse will continue to have a qualifying income interest in the trusts. Based upon the facts presented and representations made, we conclude that after the

¹No ruling has been requested concerning the *income tax* consequences of Spouse's proposed disclaimer of an income interest in Trust A, so we have not opined on the same.

division of Marital Share into Trust A and Trust B, Trust A and Trust B will continue to be QTIP trusts under § 2056(b)(7).

Rulings 3 and 4

Section 2501 imposes a tax on the transfer of property by gift. Section 2511 provides that the gift tax imposed by § 2501 shall apply whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 25.2511-2(a) of the Gift Tax Regulations provides that the gift tax is a primary and personal liability of the donor, is an excise upon his act of making the transfer, is measured by the value of the property passing from the donor, and attaches regardless of the fact that the identity of the donee may not then be known or ascertainable.

Section 2518 provides that, if a person makes a qualified disclaimer with respect to any interest in property, the disclaimed interest will be treated for gift, estate, and generation-skipping transfer tax purposes as if the interest had never been transferred to such person.

Section 2518(b) provides that a “qualified disclaimer” means an irrevocable and unqualified refusal by a person to accept an interest in property, but only if: (1) the disclaimer is in writing; (2) the disclaimer is received by the transferor of the interest, his legal representative, or the holder of the legal title to the property to which the interest relates not later than the date which is nine months after the later of (A) the date on which the transfer creating the interest in the person is made, or (B) the day on which the person attains age 21; (3) the person has not accepted the interest or any of its benefits; and (4) as a result of the disclaimer, the interest passes without any direction on the part of the person making the disclaimer and passes either to the decedent's spouse or to a person other than the person making the disclaimer.

Section 2519 provides that for gift tax purposes any disposition by the surviving spouse of all or part of a qualifying income interest for life in any property for which a deduction was allowed under § 2056(b)(7) is treated as a transfer by the surviving spouse of all interests in the property other than the qualifying income interest. The transfer of the qualifying income interest of the spouse is a transfer by the spouse subject to gift tax under § 2511. Section 25.2519-1(a).

Section 25.2519-1(c)(1) provides that the amount treated as a transfer under § 2519 upon a disposition of all or part of a qualifying income interest for life in qualified terminable interest property is equal to the fair market value of the entire property subject to the qualifying income interest, determined on the date of the disposition (including any accumulated income and not reduced by any amount excluded from total gifts under § 2503(b) with respect to the transfer creating the interest), less the value of

the qualifying income interest in the property on the date of the disposition. The gift tax consequences of the disposition of the qualifying income interest are determined separately under § 25.2511-2.

In this case, the trustee will divide Marital Share into Trust A and Trust B. At the moment of division, Spouse will retain a qualifying income interest in both trusts. After the division of Marital Share, each separate trust will be a QTIP trust under § 2056(b)(7) and the division will not be treated as a disposition under § 2519.

Spouse's disclaimer is not a qualified disclaimer for purposes of § 2518. Accordingly, based on the facts submitted and the representations made, Spouse's disclaimer of his income interest in Trust A will be treated as a disposition of his qualifying income interest in Trust A. Therefore, Spouse will make a gift of his qualifying income interest in Trust A under § 2511, and will make a gift of all of the interests in Trust A other than the qualifying income interest under § 2519.

We also conclude, based on the facts presented and representations made, that Spouse's disclaimer of his interest in Trust A will not cause any property in Trust B to be treated as a gift by Spouse under § 2519.

Ruling 5

Section 2044(a) provides that the value of the gross estate shall include the value of any property to which § 2044 applies in which the decedent had a qualifying income interest for life. Section 2044(b) provides that § 2044 applies to any property if (1) a deduction was allowed with respect to the transfer of such property to the decedent under § 2056(b)(7) or § 2523(f), and (2) § 2519 did not apply with respect to a disposition by the decedent of part or all of such property.

As stated above, Spouse's disclaimer of his interest in Trust A will result in Spouse making a gift, under § 2519, of the entire fair market value of the assets in Trust A, less the value of the qualifying income interest. Section 2044(b)(2) provides that § 2044(a) does not apply to any property if § 2519 applies to the disposition of part or all of that property prior to Spouse's death. Accordingly, based on the facts submitted and the representations made, we conclude that the value of the property in Trust A treated as transferred under § 2519 will not be included in Spouse's gross estate under § 2044(a) because of the application of § 2044(b)(2).

Ruling 6

Section 2702(a)(1) provides that solely for the purpose of determining whether a transfer of an interest in trust to (or for the benefit of) a member of the transferor's family is a gift (and the value of such transfer), the value of any interest in such trust retained by the transferor or any applicable family member (as defined in § 2701(e)(2)) shall be determined as provided in § 2702(a)(2).

Section 2702(a)(2) provides that the value of any retained interest which is not a qualified interest (as defined in § 2702(b)) shall be treated as being zero and the value of any retained interest that is a qualified interest (as defined in § 2702(b)) shall be determined under § 7520. Under § 25.2702-2(a)(3), the term “retained” means held by the same individual both before and after the transfer in trust.

In this case, Spouse will disclaim his income interest in Trust A. We concluded earlier that the disclaimer will not cause any property in Trust B to be treated as a gift by Spouse under § 2519. Accordingly, based upon the facts presented and representations made, we conclude that Spouse’s disclaimer of his interest in Trust A will not cause his interest in Trust B to be valued at zero under § 2702.

In accordance with the Power of Attorney on file with this office, we have sent a copy of this letter to your authorized representatives.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Lorraine E. Gardner
Lorraine E. Gardner
Senior Counsel, Branch 4
Office of the Associate Chief Counsel
(Passthroughs and Special Industries)

Enclosure:

Copy for § 6110 purposes

cc: